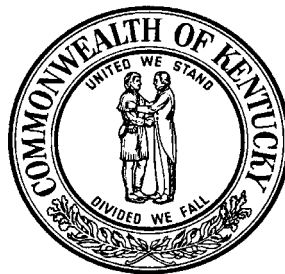


**LETTER FROM THE AUDITOR OF PUBLIC ACCOUNTS  
DEPARTMENT OF MILITARY AFFAIRS**

**In Reference to the Statewide Single Audit  
of the Commonwealth of Kentucky**

**For the Year Ended  
June 30, 2005**



**CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS  
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**CRIT LUALLEN**  
**AUDITOR OF PUBLIC ACCOUNTS**

To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Donald C. Storm, Major General KYNG  
The Adjutant General  
Department of Military Affairs

**MANAGEMENT LETTER**

KRS 43.090 (1) requires the Auditor of Public Accounts, upon completion of each audit and investigation, to prepare a report of all findings and recommendations, and to furnish copies of the report to the head of the agency to which the report pertains, and to the Governor, among others. This KRS also requires the Department of Military Affairs to, within 60 days of the completion of the final audit, notify the Legislative Research Commission and the Auditor of Public Accounts of the audit recommendations it has implemented and those it has not implemented and any reasons therefore. We are providing this letter to the Department of Military Affairs in compliance with KRS 43.090.

The work completed on the Department of Military Affairs is part of the overall opinions included in the audit of the Commonwealth of Kentucky's Comprehensive Annual Financial Report (CAFR) and Statewide Single Audit of Kentucky (SSWAK). Findings and recommendations for agencies, audited as part of the CAFR and SSWAK, if applicable, can be found in the Statewide Single Audit Report. This report can be obtained on our website at [www.auditor.ky.gov](http://www.auditor.ky.gov).

In planning and performing our audits of the Commonwealth for the year ended June 30, 2005, we considered the Department of Military Affairs' internal control over financial reporting and compliance with laws, regulations, contracts and grant agreements in order to determine our auditing procedures for the purpose of expressing opinions included in the audit of the CAFR and SSWAK and not to provide an opinion on internal control or on compliance.

However, during our audit we became aware of certain matters that are opportunities for strengthening internal controls and operating efficiency. The SSWAK is a separate report dated March 9, 2006 and contains all reportable conditions and material weaknesses in the Commonwealth's internal control structure and also contains all reportable instances of noncompliance. This letter does contain the Department of Military Affairs findings and our recommendations that have been extracted from the SSWAK report along with other matters that have been identified.



To the People of Kentucky  
Honorable Ernie Fletcher, Governor  
Donald C. Storm, Major General KYNG  
The Adjutant General  
Department of Military Affairs

We will review the status of these comments during our next audit. We have already discussed many of these comments and suggestions with various Department of Military Affairs personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Included in this letter are the following:

- ◆ Acronym List
- ◆ Schedule of Expenditures of Federal Awards
- ◆ Notes to the Schedule of Expenditures of Federal Awards
- ◆ Findings and Recommendations
  - (Other Matters and CAFR/SSWAK Findings, if applicable, excerpted from the SSWAK)
- ◆ Summary Schedule of Prior Year Audit Findings

Respectfully submitted,



Crit Luallen  
Auditor of Public Accounts

## **LIST OF ABBREVIATIONS/ACRONYMS**

ANGI	Air National Guard Regulations
APA	Auditor of Public Accounts
AYCM	Army Communications
CAFR	Comprehensive Annual Financial Report
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
Commonwealth	Commonwealth of Kentucky
CSEPP	Chemical Stockpile Emergency Preparedness Program
DMA	Department of Military Affairs
DMAR	Department of Military Affairs Regulations
DOJ/OJP	U. S. Department of Justice, Office of Justice Programs
EMA	Emergency Management Assistance
FAP	Finance and Administration Cabinet Accounting Policies
FMS	Facilities Management System
FEMA	Federal Emergency Management Agency
FY	Fiscal Year
FYE	Fiscal Year Ended
GAR	Governor's Authorized Representative
IMF	Installation Management Fund
KRS	Kentucky Revised Statutes
KyDEM	Kentucky Department of Emergency Management
MARS	Management Administrative Reporting System
MCA	Master Cooperative Agreement
MISC	Miscellaneous
NA	Not Applicable
NGB	National Guard Bureau
NGR	National Guard Regulations
PA	Public Assistance
PRIDE	Planning Resource for Infrastructure Development & Evaluation
OMB	Office of Management and Budget
RRT	Regional Response Team
SDPESP	State Domestic Preparedness Equipment Support Program
SEFA	Schedule of Expenditures of Federal Awards
SF	Standard Form
SHSGP	State Homeland Security Grant Program
SSWAK	Statewide Single Audit of Kentucky
U.S.	United States
USPFO	United States Property and Fiscal Officer
WHFRTC	Wendell H. Ford Regional Training Center
WMD	Weapons of Mass Destruction

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**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FEDERAL ASSISTANCE PROGRAMS  
FOR THE YEAR ENDED JUNE 30, 2005**

CFDA #	Program Title	Expenditures		Provided to Subrecipient
		Cash	Noncash	
DEPARTMENT OF MILITARY AFFAIRS				
U.S. Department of Commerce				
Direct Program:				
11.450	Automated Flood Warning Systems (AFWS)	\$	100,442	
U.S. Department of Defense				
Direct Programs:				
12.400	Military Construction, National Guard		3,378,550	
12.401	National Guard Military Operations and Maintenance (O&M) Projects		13,394,934	
12.404	National Guard Civilian Youth Opportunities		1,692,764	
U.S. Department of Labor				
Passed Through From Cabinet for Workforce Development:				
Workforce Investment Act Cluster:				
17.259	WIA Youth Activities		293,897	
17.267	WIA Incentive Grants - Section 503 Grants to States		7,255	
U.S. Department of Transportation				
Direct Programs:				
Air Transportation Cluster:				
20.106	Airport Improvement Program		1,295,326	
20.703	Interagency Hazardous Materials Public Sector Training and Planning Grants		224,406	
U.S. Department of Education				
Passed Through From Department of Education:				
84.002	Adult Education State Grant Program		123,959	
U.S. Department of Health and Human Services				
Passed Through From Cabinet for Health Services:				
93.003	Public Health and Social Services Emergency Fund		30,004	
93.283	Centers for Disease Control and Prevention - Investigations and Technical Assistance		196,471	
93.982	Mental Health Disaster Assistance and Emergency Mental Health		939,536	

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FEDERAL ASSISTANCE PROGRAMS  
FOR THE YEAR ENDED JUNE 30, 2005**

CFDA #	Program Title	Expenditures		Provided to Subrecipient
		Cash	Noncash	
DEPARTMENT OF MILITARY AFFAIRS				
U.S. Department of Homeland Security				
Direct Programs:				
Homeland Security Cluster:				
97.004	State Domestic Preparedness Equipment Support Program (Note 2)	15,124,107		15,012,869
97.067	Homeland Security Grant Program (Note 2)	1,014,747		146,167
97.017	Pre-Disaster Mitigation (PDM) Competitive Grants	32,321		32,321
97.020	Hazardous Materials Training Program	1,905		
97.021	Hazardous Materials Assistance Program (Note 3)	-		
97.032	Crisis Counseling	297,556		90,359
97.036	Public Assistance Grants	15,833,004		15,565,180
97.039	Hazard Mitigation Grant	2,104,203		2,064,585
97.040	Chemical Stockpile Emergency Preparedness Program	4,533,071		3,706,188
97.042	Emergency Management Performance Grants	1,376,931		962,397
97.047	Pre-Disaster Mitigation	273,672		45,891
97.051	State and Local All Hazards Emergency Operations Planning	4,932		
97.052	Emergency Operations Centers	9,336		
97.053	Citizen Corps	4,782		4,782
97.054	Community Emergency Response Teams	103,288		103,129
TOTAL DEPARTMENT OF MILITARY AFFAIRS		\$ 62,391,399	\$	37,733,868

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

**Note 1 - Purpose of the Schedule and Significant Accounting Policies**

**Basis of Presentation** - OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, requires a Schedule of Expenditures of Federal Awards showing each federal financial assistance program as identified in the *Catalog of Federal Domestic Assistance*. The accompanying schedule includes all federal grant activity for the Commonwealth, except those programs administered by state universities, and is presented primarily on the basis of cash disbursements as modified by the application of Kentucky Revised Statute (KRS) 45.229. Consequently, certain expenditures are recorded in the accounts only when cash is disbursed. The Commonwealth elected to exclude state universities from the statewide single audit, except as part of the audit of the basic financial statements.

KRS 45.229 provides that the Finance and Administration Cabinet may, “for a period of thirty (30) days after the close of any fiscal year, draw warrants against the available balances of appropriations made for that fiscal year, for the payment of expenditures incurred during that year or in fulfillment of contracts properly made during the year, but for no other purpose.” However, there is an exception to the application of KRS 45.229 in that regular payroll expenses incurred during the last pay period of the fiscal year are charged to the next year.

The basic financial statements of the Commonwealth are presented on the modified accrual basis of accounting for the governmental fund financial statements and the accrual basis of accounting for the government-wide, proprietary fund, and fiduciary fund financial statements. Therefore, the schedule may not be directly traceable to the basic financial statements in all cases.

Clusters of programs are indicated in the schedule by light gray shading.

The state agencies’ schedule is presented on the cash, modified cash, or accrual basis of accounting.

**Inter-Agency Activity** - Certain transactions relating to federal financial assistance may appear in the records of more than one (1) state agency. To avoid the overstatement of federal expenditures, the following policies were adopted for the presentation of the schedule:

- (a) Federal moneys may be received by a state agency and passed through to another state agency where the moneys are expended. Except for pass-throughs to state universities as discussed below, this inter-agency transfer activity is reported by the agency expending the moneys.

State agencies that pass federal funds to state universities report those amounts as expenditures.

- (b) Federal moneys received by a state agency and used to purchase goods or services from another state agency are reported in the schedule as an expenditure by the purchasing agency only.

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

**Note 2 - Type A Programs**

Type A programs for the Commonwealth mean any program for which total expenditures of federal awards exceeded \$20 million for FY 05. The Department of Military Affairs had one cash program that met the Type A program definition for FY 05, some of which was administered by more than one (1) state agency. The Commonwealth identified clusters among the Type A programs by gray shading. The Type A program was:

<b><u>CFDA #</u></b>	<b><u>Program Title</u></b>	<b><u>Expenditures</u></b>
<b>97.004</b>	State Domestic Preparedness Equipment Support Program	<u>\$ 15,124,107</u>
<b>Total Type A Programs:</b>		<u>\$ 15,124,107</u>

**Note 3 - Zero Expenditure Programs**

These programs had no expenditures related to the Department of Military Affairs during FY 05. The zero expenditure programs included programs with no activity during the year, such as old programs not officially closed out or new programs issued late in the fiscal year. They also included programs with activity other than expenditures.

## **FINANCIAL STATEMENT FINDINGS**

### ***Other Matters Relating to Internal Controls and/or Instances of Noncompliance***

#### **FINDING 05-DMA-1: The Department Of Military Affairs Should Implement Procedures To Comply With The Finance And Administration Procard Regulations**

The Department of Military Affairs (DMA) expended over one (1) million dollars through the ProCard Program in FY 05. We selected a random sample of 20 ProCard expenditures and noted the following:

- One (1) instance where an employee made a purchase with another cardholder's card. DMA indicated that the cardholder was unable to travel to pickup the part and the other employee was sent in his stead. According to DMA personnel and documentation, the cardholder appears to have ordered the part, but did not complete the transaction by retrieving the merchandise purchased. The employee signed the cardholder's name and their name to the credit card receipt.
- Two (2) instances where federal and state excise taxes were paid for aviation fuel. DMA personnel indicated the state had no exemption from these taxes. However, the Federal Excise Tax Handbook specifically exempts state and local governments from this tax.
- Two (2) instances where DMA did not have evidence that the good or service had been received and verified to have been completed satisfactorily.
- Two (2) instances where DMA could not produce the credit card receipt.

Failure to follow FAC's ProCard procedures may result in the revocation of cards, questionable purchases, receiving and paying for goods not received and lack of supporting documentation. Also, payment of taxes not legally due may cost the Commonwealth funds that could be used for other purposes.

FAP 111-58-00 #2 - Requires that the ProCard be used exclusively by the employee named on the card and shall not be shared or loaned to other employees.

The Federal Excise Tax Handbook and 26 USC Subpart 29.202 exempts state and local governments from special-fuels excise taxes.

FAP 111-58-00 #11 requires all cardholders to properly inspect all shipments.

FAP 11-58-00 #12 requires the agency to maintain documentation for all transactions, including the signed credit card receipt.

**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-1: The Department Of Military Affairs Should Implement Procedures To Comply With The Finance And Administration Procard Regulations (Continued)**

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**Recommendation**

We recommend DMA implement and comply with the following:

- Forbid the sharing and borrowing of cards;
- Investigate whether the Commonwealth must pay federal excise taxes on aviation fuel;
- Establish a procedure which documents the receipt of all goods and services; and
- Obtain credit card receipts for all transactions.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for PROCARD procurement activities is to provide reasonable assurance that DMA actions are in compliance with state law and published procedures. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA does not concur with the auditor's findings concerning the lack of a credit card receipt for phone purchases but does concur with the auditor's findings on the improper card-holder procedure, the Federal Excise Tax exemption, and the lack of evidence of the receipt of the goods or services.*

*For the audit finding concerning the two instances where DMA could not produce a credit card receipt, this condition was due to the purchase being made online or by telephone; thus there is no POS receipt. To record this transaction, the original vendor's invoice/receipt is annotated to indicate payment by credit card which serves as documentation of the purchase by PROCARD. Since the use of the PROCARD for online or telephonic procurement is not prohibited by state policies and procedures, DMA does not concur with the auditor's finding on this specific issue.*

**FINANCIAL STATEMENT FINDINGS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-1: The Department Of Military Affairs Should Implement Procedures To Comply With The Finance And Administration Procard Regulations (Continued)**

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**Management Response and Corrective Action Plan**

*For the audit finding concerning the improper card-holder procedure, DMA concurs with the auditor's finding and plans on the following corrective action: His supervisor will be required to counsel this individual on his job performance to insure that this cardholder will, without fail, order all parts, retrieve all parts, inspect for accuracy that the item numbers, amounts and parts are correct and insure that he is the only person that signs the credit card receipts.*

*For the audit finding concerning the two instances where federal and state excise taxes were paid for aviation fuel, DMA concurs with the auditor's finding. Since the Federal Excise Tax Handbook specifically exempts state and local governments from this tax, DMA plans on the following corrective action:*

*The Division of Air Transportation has scheduled a meeting with an Internal Revenue Service representative on Friday, March 24th to determine how we can obtain a refund for these taxes paid. Once a determination is made, we will follow up with additional response to these findings.*

*Lastly, for the audit finding concerning the two instances where DMA did not have evidence that the goods or services had been received and verified to have been completed satisfactorily, DMA concurs with the auditor's finding. DMA policy now requires all maintenance service call repair contracts to be issued, administered, verified, and paid utilizing PD procurement procedures*

**Auditor Reply**

We do not question that both instances cited may have been phone or Internet purchases, however, there was no evidence of this on the documentation provided.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-2: The Department Of Military Affairs Should Develop An Internal Control System To Comply With OMB Circular A-133 Compliance Requirements**

---

State Agency: Department of Military Affairs

Federal Program: CFDA 97.004 State Domestic Preparedness Equipment Support Program

Pass-Through Agency: U.S. Department of Homeland Security

Compliance: Subrecipient Monitoring

Amount of Questioned Costs: None

As noted in the FY 04 audit, the State Domestic Preparedness Equipment Support Program (SDPESP) did not establish the following procedures to ensure compliance with the subrecipient monitoring requirements found in OMB Circular A-133, including:

- Establishing a tracking system to determine which subrecipients were required to have an A-133 audit prepared which includes all the required components;
- Establishing a monitoring system to determine if subrecipients have established adequate internal control procedures over federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations. It should be noted that after our prior year audit finding, DMA developed a monitoring tool. This monitoring process began on July 1, 2005, covering FY 06, and consists of a three-page tool, which covers various aspects of internal control and documentation examination. We selected five (5) counties who had received SDPESP funds and examined the monitoring process to date. We found that only two (2) of the counties selected had been monitored for SDPESP and of these only the first page of the monitoring tool had been utilized.
- Performing desk reviews of A-133 subrecipient audits submitted;
- Resolving audit findings within six (6) months after receipt of the subrecipient audit report and ensuring the subrecipient took timely corrective action;
- Reconciling the amount of federal awards reported in subrecipient audits to amounts in the MARS accounting system.

DMA did not implement all procedures to ensure subrecipients complied with the audit and monitoring requirements of OMB Circular A-133. DMA did implement OMB Circular A-133 Subpart D (d) (1 and 2) during the audit period, which includes identifying federal awards made by informing each subrecipient of specific program information and advising subrecipients of requirements they have regarding federal laws, regulations and provisions of contracts or grant agreements; however, no other subparts of OMB Circular A-133 Subpart D (d) were implemented for this program.



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-2: The Department Of Military Affairs Should Develop An Internal Control System To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

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OMB Circular A-133 Subpart D (d) requires the following:

- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 (*\$500,000 for fiscal years ending after December 31, 2003*) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.
- (7) Require each subrecipient to permit the pass-through entity and auditors to have access to the records and financial statements as necessary for the pass-through entity to comply with this part.

**Recommendation**

We recommend that DMA:

- Establish procedures to comply with OMB Circular A-133 Subpart D (d) regarding subrecipient monitoring.
- Require the completion of the entire monitoring tool.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for sub-recipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to sub-recipients, sub-recipient activities are monitored, sub-recipient audit findings are resolved, the impact of any sub-recipient noncompliance on the pass-through*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-2: The Department Of Military Affairs Should Develop An Internal Control System To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

---

**Management Response and Corrective Action Plan**

*entity is evaluated, and sub-recipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance in the Kentucky Division of Emergency Management's State Domestic Preparedness Equipment Support Program.*

*Effective immediately, all KyDEM grant programs, to include the State Domestic Preparedness Equipment Support Program, shall utilize the grant's Master Agreement MARS document to incorporate all federal grant regulatory compliance information, to include OMB Circular A-133 audit and other requirements, is formally and contractually identified for sub-recipient compliance.*

*KyDEM has already issued written internal division policy #133-1, Sub-Recipient Audits / Monitoring, to establish a divisional monitoring system to determine if sub-recipients have established adequate internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations.*

*(3) Each KyDEM section responsible for the dispersion of federal grant funds, to include the State Domestic Preparedness Equipment Support Program, shall review the audits for their federal program sub-recipients, when received, to comply with OMB Circular A-133 and division policy #113-1, or later approved version. A memo record of this review shall be provided to the KyDEM Assistant Director for each sub-recipient audit reviewed no later than August 31<sup>st</sup> annually. When applicable, a management decision on the correction / non-correction of a sub-recipient audit finding will be issued the KyDEM Assistant Director within six months after the receipt of the sub-recipient audit report.*

*(4) KyDEM shall perform desk reviews of sub-recipient audit reports and to work with the sub-recipients to resolve audit findings within six months after receipt of the sub-recipient audit report and ensure the sub-recipient takes timely corrective action.*

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance***

#### **FINDING 05-DMA-2: The Department Of Military Affairs Should Develop An Internal Control System To Comply With OMB Circular A-133 Compliance Requirements (Continued)**

##### **Management Response and Corrective Action Plan**

*(5) At the end of each state fiscal year and upon receipt of sub-recipient audit reports for that year, each KyDEM section responsible for the dispersion of federal grant funds, to include the State Domestic Preparedness Equipment Support Program, shall reconcile the amount of Federal awards reported in sub-recipient audits to amounts in the MARS accounting system for the same CFDA number and period of time as the sub-recipient's audit and a memo record of this reconciliation with supporting MARS financial documents shall be provided to the KyDEM Assistant Director no later than August 31<sup>st</sup> annually.*

#### **FINDING 05-DMA-3: The Department Of Military Affairs Should Continue To Implement The Procedures Established To Fully Comply With OMB A-133 And Develop Procedures To Ensure Personnel Complete The Entire Monitoring Tool**

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 Public Assistance Program

Pass-Through Agency: U.S. Federal Emergency Management Agency

Compliance: Subrecipient Monitoring

Amount of Questioned Costs: None

The Public Assistance Program did not establish the following procedures to ensure compliance with portions of the audit and monitoring requirements found in OMB Circular A-133, including:

- Performing desk review of A-133 subrecipient audits submitted;
- Resolving audit findings within six (6) months after receipt of the subrecipient audit report and ensuring the subrecipient took timely corrective action;
- Reconciling the amount of federal awards reported in subrecipient audits to amounts in the MARS accounting system.

Establishing a monitoring system to determine if subrecipients have established adequate internal control procedures over federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations. It should be noted that after our prior year audit finding, DMA developed a monitoring tool. This monitoring process began on July 1, 2005, covering FY 06, and consists of a three-page tool, which covers various aspects of internal control and documentation examination. We selected five (5)

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-3: The Department Of Military Affairs Should Continue To Implement The Procedures Established To Fully Comply With OMB A-133 And Develop Procedures To Ensure Personnel Complete The Entire Monitoring Tool (Continued)**

---

counties who had received Public Assistance funds and examined the monitoring process to date. We found that four (4) of the counties selected had been monitored and of these, only the first page of the monitoring tool had been utilized. We also noted that various county officials had completed the monitoring tool. DMA personnel should complete the monitoring tool. DMA did review the results of the monitoring tool and issued a memo of results.

Subrecipient monitoring has been a recurring comment for DMA and in response to these comments, DMA developed detailed procedures to correct past deficiencies. Many of the items noted in the past have been corrected. However, for the items noted above, incomplete or no corrective action has been implemented.

OMB Circular A-133 Subpart D (d) requires the following:

- (3) Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six (6) months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.
- (6) Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.

**Recommendation**

We recommend DMA:

- Continue to implement the procedures established to fully comply with OMB Circular A-133.
- Develop procedures to ensure DMA personnel complete the entire monitoring tool.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-3: The Department Of Military Affairs Should Continue To Implement The Procedures Established To Fully Comply With OMB A-133 And Develop Procedures To Ensure Personnel Complete The Entire Monitoring Tool (Continued)**

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**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for sub-recipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to sub-recipients, sub-recipient activities are monitored, sub-recipient audit findings are resolved, the impact of any sub-recipient noncompliance on the pass-through entity is evaluated, and sub-recipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA concurs in part with the auditor's finding and will continue to implement its corrective action plan for the Public Assistance disaster grant program. However, DMA feels that the auditor's may have had some confusion between the two different programs identified as lacking proper sub-recipient monitoring and these inconsistent statements are detailed below.*

*There are two separate and distinct programs within DMA that have been identified as having inadequate sub-recipient monitoring. The Public Assistance (PA) disaster grant program was the first identified and developed their own program for corrective action implementation. Subsequently, in a follow-on audit, the State Domestic Preparedness Equipment Support Program (SDPESP) was identified by the auditor's as also lacking in sub-recipient monitoring and this new SDPESP finding was published as a totally separate audit finding from the PA program finding. When the SDPESP finding occurred, the DEM Assistant Director for Administrative Support stepped in and designed a sub-recipient monitoring program to address the SDPESP grant program and all the other federal grant programs (CSEPP, WMD, Title III, EMA, HM) but less the PA disaster grant program which was allowed to continue utilizing its own corrective action program. However, several of the auditor's comments in the current PA finding seems to have the two corrective action programs mixed up.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-3: The Department Of Military Affairs Should Continue To Implement The Procedures Established To Fully Comply With OMB A-133 And Develop Procedures To Ensure Personnel Complete The Entire Monitoring Tool (Continued)**

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**Management Response and Corrective Action Plan**

1. *In the “Condition” section, bullet four (4), it states that there is a three page-monitoring tool for the PA grant program. However, this “three-page” monitoring tool is the one used by the KyDEM Assistant Director for sub-recipient monitoring in all the other KyEM grant programs (SDPESP, CSEPP, WMD, Title III, EMA) but the PA sub-recipient monitoring tool is only one page long due to it covering only one grant program.*
2. *In the “Condition” section, bullet four (4), it states that the PA sub-recipient monitoring program began on July 1, 2005. This is when the KyDEM Assistant Director started his sub-recipient monitoring program for all the other KyDEM grants except the PA program grants.*

**Auditor Reply**

We apparently misunderstood the specific monitoring tools usage and the date the monitoring started. However, these misunderstandings did not affect the overall finding that DMA needs to improve their subrecipient monitoring for the Public Assistance Program. Also, allowing those monitored to complete monitoring tools themselves essentially negates any usefulness of this process.

DMA did not discuss how they plan to address the remainder of the recommendations. To reiterate, we recommend that DMA:

- Continue to implement the procedures established to fully comply with OMB Circular A-133.
- Develop procedures to ensure DMA personnel complete the entire monitoring tool.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-4: The Department Of Military Affairs Should Adhere To  
Policies Instituted For Oversight Of The Installation Management Fund Accounts**

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Program Income

Amount of Questioned Costs: None

Federal regulation NGR 5-1/ANGI 63-101 permits the rental of state-owned, federally supported armories provided that the income is used to maintain the armories. KRS 36.086 permits the establishment of an armory bank account, referred to as an Installation Management Fund, or IMF, to receive rental income and pay maintenance expenses. The federally appointed armory manager is authorized to execute rental contracts and manage the IMF. Apart from vending machine restocking, all expenditures over \$50 require prior approval from the Director of the Facilities Division. The Facilities Division also oversees the IMF by requiring a monthly report from each armory manager. This report contains a detailed listing of receipts and expenditures, a copy of the bank statement and checks, copies of rental agreements, and supporting documentation for all expenditures.

We examined every FY 05 monthly report from five (5) armories and noted the following problems:

**Improper Handling of Receipts**

- The April 2005 monthly report for the Glasgow IMF included a deposit ticket that showed the armory manager had received \$200 cash back from a \$650 check. This was overlooked in the DMA review of the report. When questioned, he stated that the cash was used to pay someone in connection with the armory rental. DMA performed no additional follow up.

**Missing Documentation for Expenditures**

- The Glasgow IMF had 14 expenditures, totaling \$834.29, without supporting documentation.

**Missing Contracts**

- The Glasgow IMF had four (4) deposits, totaling \$1,137.70, with no contracts or other supporting documentation.
- The Middlesboro IMF had three (3) deposits, totaling \$ 1,777.98, with no contracts or other supporting documentation.
- The Bowling Green armory manager reported the loss of three (3) contracts during the moving of his office space.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-4: The Department Of Military Affairs Should Adhere To Policies Instituted For Oversight Of The Installation Management Fund Accounts (Continued)**

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## Failure to Obtain Advance Approval of Expenditures over \$50

- The Bowling Green armory manager did not request approval for 27 expenditures over \$50 totaling \$3,569.97.
- The Glasgow armory manager did not request approval for six (6) expenditures over \$50 totaling \$655.05.
- The Middlesboro armory manager did not request approval for 11 expenditures over \$50 totaling \$1,229.43.

## Expenditures for Purposes Other Than Armory Maintenance

- The Glasgow IMF purchased \$33.97 in office supplies.
- The Henderson IMF purchased decorations on two (2) occasions totaling \$42.00.

## Missing Report

- Glasgow did not file an IMF report for January 2005, when the armory was between managers; however, the file at DMA did contain copies of the January bank statement and checks.

Recommendations from the fiscal year 2004 audit for dealing with problems with Program Income compliance were delivered near the end of fiscal year 2005. In response DMA adopted improved procedures, but these were not put into effect until FY 06 because of the audit's timing. Consequently, testing of FY 05 activities revealed problems similar to those noted during the FY 04 audit.

DMA is a state agency, while armory managers are federally appointed. This means that DMA personnel request cooperation but have limited enforcement power. Formerly the armory manager made all payments to individuals (typically for armory management fees or for security and cleanup in connection with armory rentals) directly from the IMF. As one of its new procedures, DMA now processes these payments through MARS. This assures that these payments are appropriately reported on form 1099-MISC to the Internal Revenue Service and the Kentucky Department of Revenue. Also, because payments are contingent upon receipt of the monthly report, this policy encourages full and timely reporting. Program income compliance should improve as a result of this change; however, DMA did not implement the new procedure until FY 06. A further complicating factor is the high turnover rate among armory managers due to widespread deployment of National Guard units.

The Glasgow armory manager took cash from a deposit and failed to document its disposition (see "Improper Handling of Receipts" above). The manager's subsequent submission of documentation supports his statement that the cash paid for a rental expense; however, initially he created the appearance of diverting the funds for personal use.



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-4: The Department Of Military Affairs Should Adhere To Policies Instituted For Oversight Of The Installation Management Fund Accounts (Continued)**

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Chapter 7-1.a. (1) of federal regulation NGR 5-1/ANGI 63-101 states, in part, “Title 10 U.S.C. 18236(c) permits States to rent out armories if the State uses the rentals to maintain the armory.”

Military Affairs policy DMAR 210-8 Section VI c. states “The Standard Voucher (AGO Ky Form 27-2) when used as a receipt record will have supporting documents attached (rental, contracts, vending deposits, bank deposits, etc.). If supporting documentation is used in the previous report, reference only is required.”

Military Affairs policy DMAR 210-8 Section VI d. requires expenditures to have supporting documentation.

Military Affairs policy DMAR 210-8 Section III c. requires prior approval for any non-recurring purchase over \$50.

Good internal control procedures require that adequate documentation be submitted to allow for the verification of all deposits and expenditures. They require particularly careful documenting of cash transactions, as was not done in the cash-back deposit. Also, these procedures would provide for adequate separation of duties and the evidence of an arms-length transaction.

**Recommendation**

The Department of Military Affairs should adhere to its newly instituted policies for oversight of IMF accounts, which appear adequate to assure compliance with program income requirements.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for program income is to provide reasonable assurance that federal grant related program income is correctly earned, recorded, and used in accordance with the federal grant program requirements. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

## FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

### *Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance*

#### **FINDING 05-DMA-4: The Department of Military Affairs Should Adhere To Policies Instituted For Oversight Of The Installation Management Fund Accounts (Continued)**

##### **Management's Response and Corrective Action Plan**

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and concurs with the auditor's findings. DMA will continue to fully implement and communicate DMA Regulation 210-8, the department's revised policy regarding the administration and management of IMF accounts, to rectify this audit finding. By doing so, the FYE 2005 audit findings of noncompliance will be rectified promptly and efficiently.*

#### **FINDING 05-DMA-5: The Department Of Military Affairs Should Provide The USPFO A Written Report Of Unliquidated Claims And Undisbursed Obligations Within Ninety Days After The End Of Grants**

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Period of Availability

Amount of Questioned Costs: None

As part of our federal compliance audit, we are required to test for proper grant closeout. Out of 15 tested, five grants expended money after the end of the grant period. The Department of Military Affairs (DMA) could not produce, written evidence showing that DMA submitted a detailed listing of unliquidated claims, undisbursed obligations, or a projected timetable of the liquidation of these claims to the USPFO by December 31st. The Commonwealth's MARS accounting system shows the following expenditures were made after this deadline:

<u>PROJECT</u>	<u>EXPENDITURES</u>
AYSC4	5,567.72
AYCM4	15,636.09
AYGM4	101,000.00
AYCM2	12,916.00
AYCM3	27,272.00
TOTAL	<u>162,391.81</u>

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-5: The Department Of Military Affairs Should Provide The USPFO A Written Report Of Unliquidated Claims And Undisbursed Obligations Within Ninety Days After The End Of Grants (Continued)**

According to the Staff Assistant, DMA discussed the information on these unliquidated claims and undisbursed obligations verbally at their quarterly update meetings with the USPFO. The USPFO representatives verbally approved the extensions. Upon DMA's request, the USPFO provided a letter dated March 2, 2006, stating which grants had been granted extensions.

Failing to have written evidence documenting timely communication of the period of availability information and obtaining written documentation of the USPFO approval could result in expenditures being ineligible for reimbursement.

Section 306(b) and (c) of the Master Agreement governing the National Guard Program states, "If unliquidated claims and undisbursed obligations arising from the State's performance of the agreement will remain 90 days or longer after the close of the fiscal year, the State shall provide a detailed listing of uncleared obligations and a projected timetable for their liquidation and disbursement no later than 31 December...costs incurred in a fiscal year which are not disclosed by the State within 90 days of the end of the fiscal year, except costs associated with unliquidated claims and undisbursed obligations arising from the State's performance of the agreement which the State has reported, shall not be eligible for reimbursement by NGB."

**Recommendation**

We recommend that DMA provide by 12/31, the USPFO a written report of unliquidated claims and undisbursed obligations as well as a timetable for their liquidation for all closed grants. Documentation evidencing the USPFO approval of these extensions should be maintained.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for period of eligibility is to provide reasonable assurance that Federal grant funds are used only during the authorized period of availability. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-5: The Department Of Military Affairs Should Provide The  
USPFO A Written Report Of Unliquidated Claims And Undisbursed Obligations  
Within Ninety Days After The End Of Grants (Continued)****Management Response and Corrective Action Plan**

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA does not concur with the auditor's finding due to the incongruent extrapolation of federal requirements in excess of the stated standard that occur in the auditor's finding.*

*FACT 1: The federal regulatory standard for dealing with un-liquidated obligations is stated in Section 306(b) of the Master Cooperative Agreement for CFDA 12.401 which states, "If un-liquidated claims and un-disbursed obligations arising from the State's performance of the agreement will remain 90 days or longer after the close of the fiscal year, the State shall provide a detailed listing of un-cleared obligations and a projected timetable for their liquidation and disbursement no later than 31 December. The USPFO shall then set an appropriate new timetable for the State to submit their final accounting".*

*a. In the auditor's Condition paragraph, Cause/Effect paragraph, and Recommendation paragraph, the auditor states that a "written" report of un-liquidated obligations is required, however, Section 306(b) does not state that the detailed listing of un-liquidated obligations must be 'written'. The notification requirement addressed in Section 306(b) requires that a detailed list of un-cleared claims be provided to USP&FO and the State meets this requirement during federal, grantor required, Quarterly Un-liquidated Review meetings for all cooperative agreements except Army O&M and Army Environmental agreements which are prepared in writing as required by USP&FO.*

*FACT 2: DMA fully complies with the Section 306(b) requirement via management methodologies required by and conducted by the federal grantor, the United States Property and Fiscal Office, as is evidenced by the USP&FO letter to the auditors dated March 2, 2006 which states, in part, that "the coordination of un-liquidated requirements is conducted in regularly scheduled meetings".*

*a. The grantor required methods includes written lists for the Army Organization and Maintenance agreement and the Army Environmental agreement, and Quarterly Un-liquidated Budget Review meetings conducted by the federal grantor and program managers in direct participation with the state program coordinators for all the remaining agreements. In summary, a copy of the written list for the Army O&M agreement and the Army Environmental agreement was*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-5: The Department Of Military Affairs Should Provide The  
USPFO A Written Report Of Unliquidated Claims And Undisbursed Obligations  
Within Ninety Days After The End Of Grants (Continued)****Management Response and Corrective Action Plan**

*provided to the auditor by DMA. The federal grantor also wrote a letter to the auditor which identified the fact that the un-liquidated items for the remainder of the agreements were identified in meetings conducted by them with the state program coordinators.*

*CONCLUSION: Since the regulatory goal of the Internal Control process is “To obtain reasonable assurance that material misstatements will not occur or will be detected on a timely basis”, all sub-processes and procedures must be designed and function in accordance with this principle. The primary function of Internal Control is to obtain ‘reasonable’ assurance and not ‘absolute’ assurance. Absolute assurance is a non-achievable goal unless unlimited resources are provided which can be dedicated to a single function. Since the March 2, 2006 USP&FO letter states that “the coordination of un-liquidated requirements is conducted in regularly scheduled meetings”, the auditor can not claim that all amounts found to be expended after 31 December 2005 were improper. DMA believes that, considering all the facts, it is apparent that ‘reasonable assurance’ is being provided by the current, federal grantor required management process. Furthermore, the auditor’s recommendation that un-liquidated obligations be provided ‘in writing’ for all cooperative agreements does not necessary reduce the risk of misstatement or increase the level of assurance above the Internal Control management process that is currently being used.*

*Also, Internal Control is further defined as a process, effected by an entity’s management and other personnel, designed to provide reasonable assurance regarding the achievement of (1) effectiveness and efficiency of operations, (2) reliability of financial reporting, and (3) compliance with applicable laws and regulations (both federal and state). This auditor’s finding fails to demonstrate that the current, federal grantor required management process materially and improperly degraded the effectiveness and efficiency of operations, the reliability of financial reporting, or was inconsistent with applicable federal or state laws and regulations. In fact, conversely, DMA feels that the current, federal grantor required management process materially aids the agency in obtaining reasonable assurance that material misstatements will not occur by identifying and coordinating un-liquidated transactions in a very timely manner. In conclusion, DMA can find no evidence of an internal control problem in this finding and does not concur with the auditor’s findings, conclusion or recommendation.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-5: The Department Of Military Affairs Should Provide The USPFO A Written Report Of Unliquidated Claims And Undisbursed Obligations Within Ninety Days After The End Of Grants (Continued)**

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**Auditor Reply**

Although we agree that section 306(b) does not require written reports to be submitted, we believe that a written list of unliquidated claims and undisbursed obligations is essential to ensuring and proving that these requirements are met. The Cooperative Agreement uses the phrase “the State shall provide a detailed listing of uncleared obligations and a project time table for their liquidation and disbursement...”. In order for a “detailed listing” to be presented to the USPFO this means that a “detailed listing” of unliquidated claims and undisbursed obligations would first have to be prepared by the Agency. DMA failed to provide any listing of unliquidated claims and undisbursed obligations during the audit even though this was requested multiple times.

If this detailed listing was prepared and presented to the USPFO, then good internal controls dictate that management would maintain this listing to demonstrate their compliance with this section of the Cooperative Agreement to prevent and protect future expenditures from becoming questioned costs.

DMA management is correct that this weakness did not “materially and improperly degrade the effectiveness and efficiency of operations.” The \$162,392 of costs identified above, however, is significant for DMA and expenditures occurring after 12/31 in future years could be for even larger amounts. Therefore, this comment is classified as a Reportable Condition and not a material weakness.

DMA has stated “the current federal grantor required management process materially aids the agency in obtaining reasonable assurance that material misstatements will not occur by identifying and coordinating un-liquidated transactions in a very timely manner.” We simply recommend that documentation of these claims (which are presented to the USPFO) be maintained and presented upon request to demonstrate compliance with the cooperative agreement.

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance***

#### **FINDING 05-DMA-6: The Department Of Military Affairs Should Establish Procedures To Ensure SF-269 Quarterly Reports Are Accurate**

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 Public Assistance Program

Pass-Through Agency: U.S. Emergency Management Agency

Compliance: Reporting

Amount of Questioned Costs: None

The Department of Military Affairs (DMA) Public Assistance program is required to submit quarterly SF-269 Reports. The preparation process involves accounting and reporting on several different projects, gathering and analyzing data from MARS reports, and making adjustments and corrections as needed.

We tested one (1) of four (4) quarterly SF-269s and found the Public Assistance program personnel did not establish effective internal control over accounting, preparing, gathering, and analyzing data from MARS. As noted below, DMA miscalculated or mistyped the state-share-amount of total outlays on its SF-269 reports and issued the reports without detecting the errors:

Disaster #	State Share amount on SF-269 Report	State Share amount from MARS	Difference
1320	760,878.48	774,678.77	(13,800.29)
1407	1,665,401.62	2,997,121.40	(1,331,719.78)
1454	8,474,979.87	7,030,908.64	1,444,071.23
1471	1,246,690.08	1,249,690.08	(3,000.00)

Failure to establish effective internal controls relating to the preparation and review of financial reports may lead to significant errors. These errors, if undetected, may lead to erroneous assumptions, reimbursements and reports. Inadequate management review can also lead to discrepancies.

44 CFR- Section 13.41 states that “Grantees will use Standard Form 269 or 269A, Financial Status Report, to report the status of funds for all nonconstruction grants and for construction grants when required . . .”

#### **Recommendation**

DMA should prepare detailed written procedures for all required processes. These procedures should include instructions on reconciling the report contents to MARS and having supervisor review. The written procedures would also allow replacement employees or management to continue performing crucial processes in a consistent manner.

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance***

#### **FINDING 05-DMA-6: The Department Of Military Affairs Should Establish Procedures To Ensure SF-269 Quarterly Reports Are Accurate (Continued)**

##### **Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for federal grant reporting is to provide reasonable assurance that the reports of Federal grant awards submitted to the Federal awarding agency or pass-through entity include all activity of the report period, are supported by underlying accounting or performance records, and are fairly presented in accordance with Federal grant program requirements. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that we concur with the auditor's findings.*

*The 97.036 SF-269 reports for quarters ending 4/1/05-6/30/05 and 7/1/05-9/30/05 have been corrected and submitted to FEMA for inclusion in their records.*

*Procedures will be added to the KyEM's Administrative Policy on How to Prepare SF-269 Reports for 97.036 by COB 4/15/06 to include the following steps:*

- *KyEM's Administrative Section Supervisor will prepare reports and will attach the adding machine tape and copy of the reports used to get the amounts.*
- *Reports and attachments will be handed over to Program Manager of 97.036, to review.*
- *Reports and attachments will then go to the Assistant Director of Administrative Services, to review and approve before signing.*
- *A cover sheet will be developed to go on file with the SF-269 reports to show the following:*
  - *Reports prepared by: \_\_\_\_\_, Administrative Section Supervisor*
  - *Reports reviewed by: \_\_\_\_\_, Program Manager*
  - *Reports reviewed, approved and signed by: \_\_\_\_\_, Assistant Director*

*All policy changes will be effective beginning with quarter ending 3/31/06.*



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-7: The Department Of Military Affairs Should Reimburse The Federal Government For Questioned Costs And Request Reimbursement Only For Expenditures That Have Adequate Supporting Documentation**

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Allowable Cost

Amount of Questioned Costs: \$40,188

While testing a sample of ten (10) PX documents, we tested PX000001780, which charged \$40,188.00 to the federal government for telecommunication charges that allegedly were not paid between 10/1/01-9/30/03. We were informed that the amount transferred was determined by conducting a review of all of the telecommunications charges that were paid during the above referenced time period. To verify the accuracy of the amount transferred, we extracted a MARS report of the telecommunications charges during this period, sorted it by activity code, fiscal year, and fiscal month, and we estimate that around 41.4% of the AYCM2 and 46.2% of the AYCM3 charges had already been paid (usually in another activity code or were simply overlooked). In addition, while testing E262 telecommunication charges in another section of the audit, we came across several bills with (sometimes large) prior month balances. This would indicate that sometimes the monthly invoices are not paid. Since some of the invoices were already paid in another activity code and other invoices were either not paid or overlooked (which means that would be paid later) this would suggest that a draw down has already occurred or will occur for these expenses. The transfer of charges on this PX document then results in the same expenditure being reimbursed twice.

Our understanding is that the federal funds were charged for the amounts listed above because the appropriations were about to expire and the funds would have to be used or they would be forfeited. Based upon our review, since we believe many of the telephone charges were already paid for in another activity code or were overlooked during the agency review and since we believe the majority of the other expenses were paid for later, this transfer essentially results in the state receiving reimbursement twice for the same expenditure.

Good internal controls dictate that adequate supporting documentation be maintained to justify expenditures of federal funds. In addition, internal controls should be in place to prevent double reimbursements for the same expenditure.

**Recommendation**

We recommend that Military Affairs 1) reimburse the federal government for the questioned costs noted above and 2) only request reimbursement for expenses that have adequate supporting documentation (such as an invoice).

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-7: The Department Of Military Affairs Should Reimburse The Federal Government For Questioned Costs And Request Reimbursement Only For Expenditures That Have Adequate Supporting Documentation (Continued)****Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that, without a list of transaction ID's from the auditor, DMA cannot verify the auditor's claim that "the same expenditure" was "reimbursed twice", however, neither can DMA refute the claim. The federal grantor initiated the 'one-time' questioned transaction based on federal records and source documentation. The auditor did not find the federal source documentation sufficient and questioned the federal payment to the state. DMA will request that the federal grantor review this audit finding and provide instructions concerning the questioned cost.*

**Auditor Reply**

A list of transaction numbers was not provided to DMA because 1) all of the transaction numbers were available in MARS and 2) there were thousands of transaction numbers involved. We did, however, provide DMA with the exact procedures used to verify this expenditure for their response and corrective action plan.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-8: The Department Of Military Affairs Should Review Employee Approval Authorities**

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State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Activities Allowed/Allowable Cost

Amount of Questioned Costs: None

While reviewing the document approvals that were applied in MARS for a sample of ten (10) PX documents, we noticed that one individual entered and approved three (3) PX documents. No other electronic approvals from agency personnel were applied to the document in the accounting system. We did, however, review the transaction's supporting documentation (in hard copy) and found that other users were aware of and approved the transactions.

This particular user is the administrator of MARS for the agency and he acknowledged that he has this authority and can correct/re-approve these types of documents since they do not result in a disbursement. Although a disbursement is not made to a vendor, these documents essentially transfer money between the state and federal funds.

Since the user is the MARS administrator for the agency, apparently his authority is set up in the system to allow him to enter and approve certain types of transactions. Without having multiple users involved electronically with a transaction, it is possible that a user could enter and approve an unauthorized or inappropriate transaction in MARS, which could have many adverse consequences.

Good internal controls dictate that all transactions be properly authorized and that no single user has the authority to enter and approve a transaction in the accounting system.

**Recommendation**

We recommend that the Department of Military Affairs MARS administrator's approval authority be updated so that he can only enter or approve transactions in MARS. In addition, we recommend that Military Affairs review the approval authority for employees to ensure that a single user does not have the ability to both enter and approve a transaction in MARS. Finally, we recommend that the MARS administrator's supervisor review all transactions entered and approved exclusively by the MARS administrator to ensure the appropriateness and necessity of the transactions.

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance***

#### **FINDING 05-DMA-8: The Department Of Military Affairs Should Review Employee Approval Authorities (Continued)**

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##### **Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA does not concur with the auditor's finding due to factual misstatements that occur in the auditor's finding.*

1. *FACT: No single MARS user can both create and enter a transaction and then approve that same transaction because the basic security within the MARS accounting system will not allow this to occur. FACTUAL MISTATEMENT: The auditor states in the Cause and Effect paragraph, in the Criteria paragraph and in the Recommendation paragraph of the finding that a 'single user' can "both enter and approve a transaction in the accounting system". This is categorically untrue.*

*EXPLANATION: The fundamental security inherent in the MARS accounting system requires at least two MARS users to fully process an agency level transaction document (i.e. a MARS transaction requiring a document creator and up to three agency levels of approval) or a Finance Cabinet level disbursement document (i.e. a MARS transaction requiring a document creator, up to three levels of agency approval, and up to two additional FAC or GOPM level approvals). In accordance with FAC MARS security policy, the use of the full agency level approval role is as needed by the agency. The use of all three levels of agency approval is restricted by this agency to the agency administer role. The use of this restricted agency level approval function allows for efficient correction of agency level documents and their subsequent re-approval without compromising the basic accounting principle two-person rule or allowing incorrect transactions to post into the accounting system necessitating subsequent Journal Vouchering to correct the error.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-8: The Department Of Military Affairs Should Review Employee  
Approval Authorities (Continued)**

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**Management Response and Corrective Action Plan**

2. *FACT: MARS PX documents do not transfer money, cash, expenditures, allotment or anything else between state funds and federal funds. FACTUAL MISTATEMENT: The auditor states in the Condition paragraph that the MARS PX “documents essentially transfer money between the state and federal funds.” This is categorically untrue.*

*EXPLANATION: A MARS PX document is a non-accounting charge that does not appear on the General Ledger in MARS. The PX document is generally used to record indirect transactions for a billable project and is used to make adjustments. These adjustments are supported by the source documents attached to the PX. MARS PX documents are not subject to budgetary or preceding document controls that govern accounting transactions and the data is stored on the extended Project Ledger (PRJBIL) but not on the General Ledger (GENLED).*

*CONCLUSION: Internal Control means a process, effected by an entity’s management and other personnel, designed to provide reasonable assurance regarding the achievement of (1) effectiveness and efficiency of operations, (2) reliability of financial reporting, and (3) compliance with applicable laws and regulations (both federal and state). This auditor’s finding fails to demonstrate that the approval ability of the agency’s administrator to provide all three levels of agency approval on MARS documents materially and improperly affected the effectiveness and efficiency of operations, the reliability of financial reporting, or was inconsistent with applicable federal or state laws and regulations. In fact, conversely, DMA feels that this function materially aids the agency in obtaining reasonable assurance that material misstatements will not occur by detecting and correcting transactions in a very timely manner. In conclusion, DMA can find no proof of an internal control problem in this finding and does not concur with the auditor’s findings, conclusion or recommendation.*

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### ***Reportable Conditions Relating to Internal Controls and/or Reportable Instances of Noncompliance***

#### **FINDING 05-DMA-8: The Department Of Military Affairs Should Review Employee Approval Authorities (Continued)**

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##### **Auditor Reply**

1. This control weakness would seem to be a function over form issue. Although MARS security may not allow a single user to enter and approve a transaction in MARS, if the agency administrator has the ability to unapprove first level entries, make any desired changes (vendor, amount, accounting string, etc.) to the document, and then apply all levels of approval without any other agency personnel being involved, this essentially has the same effect of only having one person involved in the transaction.
  
2. Although DMA management is correct that PX documents do not appear on the General Ledger table in MARS, this does not mean that they do not have an accounting impact. For the PX documents tested, expenditures were “moved” to the project-billing table which resulted in draw downs of federal funds for these “charges.” The net effect of these transactions is that Fund 1200 expenditures were increased, which resulted in drawdowns of federal funds, which does ultimately impact cash and revenues on the general ledger table.
  
3. The purpose of this finding is not to “demonstrate that the approval ability of the agency’s administrator . . . materially and improperly affected the effectiveness and efficiency of operations, the reliability of financial reporting, or was inconsistent with applicable federal or state laws and regulations.” This finding is not a material weakness in internal control but is a reportable condition, which requires communication to management. Although good internal controls dictate that no single user have the ability to process a document without other parties being involved (and the agency MARS administrator effectively has this ability since he can unapproved 1<sup>st</sup> level approvals, make changes, and apply all remaining approvals for the agency), if this authority is essential to DMA operations, the compensating control recommended above of having “the MARS administrator’s supervisor review all transactions entered and approved exclusively by the MARS administrator to ensure the appropriateness and necessity of the transactions” periodically would be sufficient. In addition, since DMA management stated above “MARS PX documents are not subject to budgetary or preceding document controls that govern accounting transactions” this indicates a greater need to have additional parties review these transactions.

Should management decide that a periodic review of the agency MARS administrator’s transactions described above (1<sup>st</sup> level approvals are removed and changes are made) is not necessary, this would indicate a more significant internal control environment and monitoring weakness for DMA.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-9: The Department Of Military Affairs Should Require Applicants File Extension Requests Before The Initial Deadlines Recorded On Project Worksheets**

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State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 Public Assistance Program

Pass-Through Agency: U.S. Federal Emergency Management Agency

Compliance: Period of Availability

Amount of Questioned Costs: None

DMA did not have procedures in place to monitor subgrantee projects to determine if extensions are required. Federal Emergency Management Agency (FEMA) regulations set time limits for completing projects. FEMA measures these time limits from the declaration date of the major disaster or emergency and on the type of work—debris clearance - 6 months, emergency work – six (6) months and permanent work - 18 months. DMA can grant extensions, with limits similar to above deadlines, in situations of extenuating circumstances. Applicants are required to request extensions from DMA according to the Local Disaster Agreement signed between DMA and the applicant. The request for extension should be specified by project and justification should be based on circumstances beyond the control of the applicant. If applicants request time extensions beyond the limit of the DMA's authority, DMA must submit the request to FEMA for approval.

DMA tracks subgrantee payments by applicant. An applicant may have several different projects, with varying lengths of time allowed to complete the work. DMA chooses to grant extensions retroactively based upon the close out of applicant projects. DMA states that tracking the close dates on all projects they administer would be a monumental task. However, by not tracking these projects and ignoring federal regulations regarding extensions DMA puts federal funding for localities in need of assistance in jeopardy.

Applicants should only be reimbursed for costs incurred up to the latest approved completion date for a particular project. As allowed by federal regulations, DMA advances funds to applicants upon approval, for small projects. However, for large projects, DMA reimburses as the project progresses, based on periodic requests for funds. DMA does not pay administrative costs to the applicant until they close the project.

The Local Disaster Agreement signed by DMA and the subgrantee states "The applicant agrees to complete debris clearance or emergency work within six (6) months and permanent work within 18 months of the date of the declaration of a major disaster or emergency. Time extensions may be granted on an individual project basis, in accordance with 44-CFR-206-204. If an extension request is denied, the Applicant may be reimbursed for eligible project costs incurred up to the latest approved completion date. Failure to complete the project will result in the denial for funding for that project. If the project goes over the completion date and the applicant fails, to request a time extension, funding for this project may be denied."

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-9: The Department Of Military Affairs Should Require Applicants File Extension Requests Before The Initial Deadlines Recorded On Project Worksheets (Continued)**

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44 CFR 206-204 (c) states “Time limitations for completion of work-- (1) Deadlines. The project completion deadlines shown below are set from the date that a major disaster or emergency is declared and apply to all projects approved under State disaster assistance grants. Completion Deadlines: Debris clearance—6 months, Emergency work—6 months, Permanent work—18 months.”

**Recommendation**

We recommend DMA:

- Reemphasize the importance of meeting the completion deadlines and submitting extension requests when needed.
- Withhold funding to applicants who fail to submit timely extensions as required by regulations.
- Develop a procedure for monitoring project completion dates.  
Investigate the feasibility of interfacing with the Federal NEMIS database to track projects more accurately.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for period of eligibility is to provide reasonable assurance that Federal grant funds are used only during the authorized period of availability. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA does not concur with the auditor's findings.*

*Public Assistance eligible applicants (County, City, Government Agency, others) are responsible for requesting a time extension on their disaster repair projects when project work cannot be completed by the project completion deadline. But very often an extension is granted retroactively due to circumstances beyond their control. These circumstances could be related to the availability of qualified*



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-9: The Department Of Military Affairs Should Require Applicants File Extension Requests Before The Initial Deadlines Recorded On Project Worksheets (Continued)**

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**Management Response and Corrective Action Plan**

*contractors or equipment, weather delays, another disaster situation which follows the original situation, and administrative delays due to federal grantor inspection, audit and payment procedures. The auditors failed to understand that just because a disaster application has not been closed, it does not mean that specific repair projects within that application hasn't been closed for reimbursement eligibility purposes per the FEMA project deadlines. The disaster application can still be open awaiting final settlement but does not need an extension on the repair projects within that application just because the application is still open. The application could be waiting for a final inspection to be completed or something of that nature causing the application not to be closed.*

*However, to re-invigorate the currently existing internal controls, DMA plans on providing more emphasis and review on the following:*

- Reemphasize to the applicant the importance of meeting the project completion deadlines and submitting project extension requests when needed. This is already being done in the state and local agreement (when applicant briefings are held they are reminded of the project deadlines); it is in the Code of Federal Regulations 44 or CFR 44 that is provided to them; it is in the Public Assistance Guide FEMA 322 which is also provided to them; it is in the Applicant Handbook FEMA 323 which, again, is provided to them; and finally we already send out a reminder to each applicant around the established project completion dates, etc.*
- Withhold funding to applicants who fail to submit timely project extensions as required by regulations. Per FEMA CFR 44, FEMA 323, and FEMA 322 funds on small projects are paid upon approval of the project worksheet by FEMA. However, DMA's current review and final settlement procedures, that are already in place, do not allow for payment of project work that has unjustifiably exceeded the regulatory project deadlines*
- Review procedures for monitoring project completion dates. Procedures are already in place that are in keeping with DMA's resource constraints. Attached is a copy of an example letter than has been used for many years.*
- Investigate the feasibility of interfacing with the Federal NEMIS database to track projects more accurately. DMA has reviewed this suggestion from the auditor and deems it not feasible at this time.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Reportable Conditions Relating to Internal Controls and/or  
Reportable Instances of Noncompliance*****FINDING 05-DMA-9: The Department Of Military Affairs Should Require Applicants File Extension Requests Before The Initial Deadlines Recorded On Project Worksheets (Continued)**

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**Auditor Reply**

The management's response above stated that "The auditors failed to understand that just because a disaster application has not been closed, it does not mean that specified repair projects within that application hasn't been closed for reimbursement eligibility purposes per the FEMA project deadlines. The disaster application can still be open awaiting final settlement but does not need an extension on the repair projects within that application just because the application is still open."

We do understand that an applicant can have several projects, both small and large, within a disaster. However, it is incumbent upon the Department of Military Affairs to monitor all projects and ensure that applicants request extensions as necessary and as required by federal regulations quoted within the body of the finding. Applicants that do not request extensions timely should not be reimbursed the federal funds.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-10: The Department Of Military Affairs Should Ensure All Appropriate Approvals Are Obtained Prior To Processing Expenditure Transactions**

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 Public Assistance Program

Pass-Through Agency: U.S. Federal Emergency Management Agency

Compliance: Activities Allowed/Allowable Costs

Amount of Questioned Costs: None

The Department of Military Affairs (DMA) expended \$15,558,282 in public assistance funds for FY 05. We tested a sample of 40 expenditures for compliance with federal requirements and noted two (2) transactions totaling \$44,205.35 (federal share 38,108.06), without the Governor's Authorized Representative's (GAR) approval initials on the "advanced payment of funds" worksheets. DMA, as allowed by federal regulations, makes advance payments on "small" projects and reimburses applicants for "large" projects as the applicant incurs the costs and submits invoices for reimbursement. Payments should not be distributed without the appropriate approvals. DMA's internal control system did not detect the missing approvals prior to preparing and processing the payments. These payments were properly approved in the MARS system, however the GAR signature was missing on a pre-audit form.

Failure to enforce effective internal controls relating to different levels of approval may lead to payments being made in error. These errors, if undetected, may lead to erroneous reimbursements.

OMB Circular A-87 Part C 1 c requires expenditures to be properly authorized. DMA has developed policies and procedures that require the GAR or recovery supervisor to approve disbursements on the "advanced payment of funds" worksheet.

**Recommendation**

DMA should enforce current internal controls in place to ensure all appropriate approvals are obtained prior to processing expenditure transactions.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-10: The Department Of Military Affairs Should Ensure All Appropriate Approvals Are Obtained Prior To Processing Expenditure Transactions (Continued)**

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**Management Response and Corrective Action Plan**

*full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA concurs with the auditor's finding that the GAR failed to initial an information worksheet to indicate that he had been informed of the pending transaction but DMA does not concur that the payment was made inappropriately.*

*DMA agrees with finding that the GAR did not initial the DEM internal "worksheet". This DEM internal "worksheet" is used only within the Recovery Section to report payment amounts being contemplated thru MARS the official accounting system of the Commonwealth of Kentucky, other information pertaining to the payment, and for our records only. This "worksheet" is not forwarded with the MARS payment paperwork (P1, P3, Invoice, etc) to pre-audit for additional fiscal processing/approval of MARS payment documents. Of the two transactions cited by the auditor as missing the GAR's initials, the PA Officer did sign off on the "worksheet" therefore the worksheet did have one level of internal DEM staffing on it. The Recovery Supervisor will remind appropriate personnel of the internal notification process in place and to make sure that all required personnel are notified prior to submitting grant payments and other supporting documentation to Pre-Audit for fiscal processing.*

*DMA does not agree that the payments from the two transactions cited by the auditor resulted in a fiscal payment that lacked appropriate approvals. Fiscal approval of MARS transaction documents constitutes three levels of automated approval within DMA of which, the division has the first two approvals to properly record those individuals who have the legal authority to authorize the disbursement of funds. These three approvals constitute the authority for fiscal disbursement and no other paper document, checklist, or other non-MARS type document is authorized to legally record this fiscal information. If the GAR is to 'go on record' as having authorized the disbursement of funds, then that 'record' can only occur by the GAR applying division level automated approvals to the disbursement document within the MARS accounting system. (For six years, the GAR has been an approved MARS user and has always had the requisite division level approval in MARS to 'approve' these fiscal transactions.)*

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-DMA-10: The Department Of Military Affairs Should Ensure All Appropriate Approvals Are Obtained Prior To Processing Expenditure Transactions (Continued)**

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##### **Management Response and Corrective Action Plan**

*CONCLUSION. DMA can find no evidence that fiscal payments were disbursed without the appropriate approvals. Only the MARS automated approval record meets the requirement of OMB Circular A-87, Part C(1)c which requires that all "expenditures" be properly authorized. Since no paper document is authorized to legally record these MARS automated approvals, no fiscal payments were disbursed without appropriate approvals.*

##### **Auditor Reply**

When an agency represents to us that a specific internal control has been established, we assume that these controls were implemented for a particular purpose or need. In our comment, we mention that the transactions were properly approved in MARS; however, DMA did not follow their own specific internal controls. If the control has no purpose, we recommend that this process be eliminated.

#### **FINDING 05-DMA-11: The Department Of Military Affairs Should Improve Internal Controls Relating To Equipment Management**

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State Agency: Department of Military Affairs

Federal Program: CFDA 97.004 State Domestic Preparedness Equipment Support Program  
 Pass-Through Agency: U.S. Department of Homeland Security

Compliance: Equipment and Real Property Management

Amount of Questioned Costs: None

Federal statute 28 CFR 66.32 requires each Regional Response Team (RRT) to submit a semi-annual report, which lists the equipment purchased with State Domestic Preparedness Equipment Support Program funds. This detailed report should include a description, serial #, location, quantity, date purchased, condition and which area manager physically examined the equipment. In our test of the fourteen RRT's we noted the following exceptions with our review of the equipment reports:

- Region One and Region 10 did not list who physically examined the equipment;
- Region Two did not list the serial #'s, location, quantity, condition and who physically examined the equipment;
- Region Three did not record the serial #'s, quantity, purchase date, condition and who physically examined the equipment;
- Region Four and 12 did not list condition and who physically examined the equipment;

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-11: The Department Of Military Affairs Should Improve Internal Controls Relating To Equipment Management (Continued)**

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- Region Five did not list condition, purchase date and who physically examined the equipment;
- Region Six did not list serial #'s, condition, purchase date and who physically examined the equipment;
- Region Seven did not list condition, quantity and who physically examined the equipment
- Region Eight did not list location of equipment;
- Region Nine did not list quantity and who physically examined the equipment
- Region 11, 13 and 14 did not list serial #'s, location, condition, purchase date and who physically examined the equipment.

In addition, Military Affairs has still not developed procedures for the disposal of equipment purchased. The equipment is now at least one year old and we believe this procedure should be developed and disseminated to the regional response teams and local governments. Having this procedure in place would ensure any proceeds from sales were properly accounted for.

Similar problems were noted in our FY 04 audit report.

The Regional Response Teams (RRT's) are not completing the equipment reports as required by Military Affairs. Our audit covers the third semi annual equipment report and indicates the RRT's are not providing the information needed for filing complete equipment reports.

The equipment purchased is new or still under warranty so the agency does not have a have a disposal procedure in place.

Equipment reports should include all requirements of both Military Affairs and federal regulators. 28 CFR 66.32 (d) (1) requires property records to include among other things the serial number and condition of the equipment. Also, the Military Affairs program administrator has instructed the RRT's to record who physically examined each piece of equipment.

28 CFR 66.32 (e) discusses the disposition of federal property, which implies that a procedure should be in place to ensure compliance with stated statutes.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-11: The Department Of Military Affairs Should Improve Internal Controls Relating To Equipment Management (Continued)**

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**Recommendation**

We recommend Military Affairs:

- Inform the RRT's of the importance of filing a complete equipment report; and
- Develop a procedure for the disposition of equipment, distribute and inform the RRT's of this policy.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for federal grant acquired equipment is to provide reasonable assurance that proper records are maintained for equipment acquired with Federal grant awards equipment is adequately safeguarded and maintained, disposition or encumbrance of any equipment is in accordance with Federal grant requirements, and the Federal awarding agency is appropriately compensated for its share of any property sold or converted to other use. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA agrees with this finding.*

*To correct the problem, a draft Agency Policy has been written and submitted to the DEM Assistant Director for Administration for review and approval. This policy codifies KyEM's previously verbal directions concerning the inventory and reporting of equipment purchased under the Department of Homeland Security, State Homeland Security Grant Programs. The policy also includes instructions concerning the disposition of equipment, as directed under 28 CFR Chapter 1, Part 66.32 and as agreed to in Regional Response Teams' by-laws. The draft policy has been attached for review.*

## FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-DMA-12: The Department Of Military Affairs Should Improve Internal Controls Relating To The Review Process For The OJP 4587/1 Form Semi-Annual Report**

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State Agency: Department of Military Affairs

Federal Program: CFDA 97.004 State Domestic Preparedness Equipment Support Program

Pass-Through Agency: U.S. Department of Homeland Security

Compliance: Reporting

Amount of Questioned Costs: None

As noted in the prior audit, the FY 2002 State Domestic Preparedness Program Guidelines and Application Kit, the FY 2003 U. S. Department of Homeland Security, Office of Domestic Preparedness Program Guidelines and Application Kit and the FY 2003 State Homeland Security Grant Program-Part II (SHSGP II) require the submission of a semi-annual OJP Form 4587/1 Progress Report. This report provides an update of the equipment purchase for each grant during the applicable six (6)-month period. We agreed amounts from the tracking workpapers (which had been agreed to MARS) to the 4587/1 for each of the three (3) open grant reports filed covering the period January 1, 2005 through June 30, 2005 and noted the following:

#### 4587/1 Report for FY 2002 State Domestic Preparedness Equipment Program

- One (1) instance, totaling \$399.00, where DMA omitted from the 4587/1 Report, a payment made to the wrong region.

#### 4587/1 Report for FY 2003 State Domestic Preparedness Equipment Program

- One (1) instance, totaling \$624.00, where DMA recorded the amount of equipment purchased incorrectly.
- One (1) instance, totaling \$2,742.50, of equipment purchased during the report period not being listed on the 4587/1 Report.

#### 4587 Report for FY 2003 State Domestic Preparedness Equipment Program (SHSGP II)

- One (1) instance, totaling \$139.14, of equipment purchased during the report period not being listed on the 4587/1 Report.
- One (1) instance, totaling \$174.66, where the amount of equipment purchased was incorrect.
- One (1) instance, totaling \$1,500.00, where funds were returned, redeposited, and not included on the tracking workpapers. The equipment purchased should not have been included on the 4587/1 Report.

Per agency personnel, Military Affairs paid the incorrect amount (\$399.00) to the wrong region. The error has not been corrected on the 2002-4587/1 report because DMA uses delivery orders for the 2002 State Domestic Preparedness Equipment Program Payments. However the grant had been closed and a separate invoice will need to be issued to the correct region for the \$399.00.



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-12: The Department Of Military Affairs Should Improve Internal Controls Relating To The Review Process For The OJP 4587/1 Form Semi-Annual Report (Continued)**

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The \$624.00 and \$174.66 errors resulted from agency personnel focused on the total amount expended for a particular region rather than the individual amounts. The total amounts expended for each grant within the region remained the same, however, the individual amount for each of these expenditures were incorrect.

The \$1,500.00 equipment included on the 4587/1 report omission on the tracking workpapers was due to the funds being returned and redeposit and deemed to have not actually been expended.

The remainder of the exceptions (\$2,742.50 & \$139.14), DMA omitted these items from the 4587/1.

DMA management did not perform a thorough documented review/comparison of the amounts recorded on the 4587/1 report against the MARS.

We noted similar problems in the FY 04 audit.

FY 2003 U. S. Department of Homeland Security, Office of Domestic Preparedness Program Guidelines and Application Kit and FY 2003 State Homeland Security Grant Program-Part II (SHSGP II) require the submission of OJP Form 4587/1 Progress Reports that reflect accurate data and have been properly approved. An in-depth review by management prior to submission of the reports helps ensure accuracy.

Good internal control requires that management develop procedures to ensure the correctness of reports prepared and submitted.

**Recommendation**

We recommend that Military Affairs establish procedures for a documented independent management review of the 4587/1 Reports.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for federal grant reporting is to provide reasonable assurance that the reports of Federal grant awards submitted to the Federal awarding agency or pass-through entity include all activity of the report period, are supported by underlying accounting or performance records, and are fairly presented in*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-12: The Department Of Military Affairs Should Improve Internal Controls Relating To The Review Process For The OJP 4587/1 Form Semi-Annual Report (Continued)**

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**Management Response and Corrective Action Plan**

*accordance with Federal grant program requirements. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies. Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA agrees with this finding.*

*The original purpose of the separate tracking spreadsheet was to assist in managing a combined grant Master Agreement that had combined the first three grants from the Department of Justice, Office of Justice Programs State Domestic Preparedness Programs. The combined grants were not entered as separate delivery orders in MARS and therefore the tracking spreadsheet was required as a detailed expenditure by grant internal worksheet. With the final expenditures of those earlier grants the spreadsheet is no longer necessary and has only served to cause confusion when compared to the tracking reports from MARS. The FY2003 State Homeland Security Grants Part I and Part II have had their projects listed as separate delivery orders and therefore lend themselves to tracking through MARS, rather than having to track through a separate spreadsheet. To avoid any further confusion in reporting to DHS and to simplify internal reporting the separate spreadsheet will be abandoned and only the MARS reports will be used to track expenditures. This will allow for a more streamlined review of the final OJP 4587/1 by the KyEM Administrative Branch and ensure a more reliable accounting of expenditures. This procedure will be implemented with the June 2006 OJP 4587/1 Report.*

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-13: The Department Of Military Affairs Should Consider Using One Work Order System That Will Interface With The Commonwealth's Accounting System**

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State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Matching, Level of Effort, Earmarking

Amount of Questioned Costs: None

The Department of Military Affairs (DMA) work order system is fragmented and inconsistently utilized. Much of the data used relating to matching – Agreement Support Code and match rate – appears in the work order system but not in MARS. This complicates assessing compliance with federal matching requirements.

DMA uses several work order systems. Most Army Guard projects use a database provided by the Department of Defense. However, the Wendell H. Ford Regional Training Center has developed a work order system of its own. Bluegrass Station and the Air Guard also use separate systems.

Securing the approvals required in the work order system takes some time, but many Army environmental projects are emergency situations requiring reestablishment of compliance before the day is over. Consequently, to avoid delays many Army environmental projects are never entered in the work order process.

This fragmentation and inconsistent utilization deprives DMA of many of the potential benefits from a work order system. The physical records are located in several widely separated locations around the state, and the computer systems for the different work order systems are incompatible. This renders research on the performance of any particular vendor difficult, and the absence of records in the work order system on many environmental projects means there can be no assurance that such research is complete. Furthermore, the present process hinders DMA's ability to monitor activities and project progress.

Good internal controls dictate uniform usage of systems. Agencies should use one system to process vital data; multiple systems create access problems, duplication of effort, loss of comparability, and inefficiency in processing information.

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-13: The Department Of Military Affairs Should Consider Using One Work Order System That Will Interface With The Commonwealth's Accounting System (Continued)**

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**Recommendation**

The Department of Military Affairs should:

- Use a single work order system database. Implementation of the unified system should involve the users of all present systems in order to include all needed features and to maximize cooperation.
- Investigate creating an interface between MARS and the work order system. This would minimize duplication of effort.

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable costs is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the cost of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that we concur in part with the auditor's finding on Environmental work orders but do not concur with the auditor's finding on multiple work order systems.*

*The Department of Military Affairs (DMA) agrees that the separate work order systems used by the different areas of operation may appear fragmented; however, physical boundaries and the purpose of using work order systems are dependent upon whether each location has skilled trade employees to perform the maintenance and repair of the facilities located in the area. These work order systems are intended as a management tool to assess and prioritize maintenance and repair tasks and not as an accounting system. Each of these work order systems provide suitable support documentation to facilitate appropriate expenditures against reimbursable and non-reimbursable activities occurring within the accounting system. DMA has investigated the possibility of having an interface from the MARS accounting system; however, numerous issues prevent that from occurring at this time.*

## **FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-DMA-13: The Department Of Military Affairs Should Consider Using One Work Order System That Will Interface With The Commonwealth's Accounting System (Continued)**

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##### **Management Response and Corrective Action Plan**

*Notwithstanding the above, DMA is in the process of determining if the Department of Defense PRIDE (Planning Resource for Infrastructure Development and Evaluation) Work Order system may be a viable work order system for use on a universal basis. The Wendell H. Ford Regional Training Center (WHFRTC) will be the test environment for determining the functionality and practicality of the system for possible use by other areas within DMA. Training for staff at WHFRTC is tentatively scheduled to occur in late March 2006 after which the evaluation of this concept will be an on-going process.*

*Finally, a number of environmental projects are being entered in the Facilities Management System (FMS) work order system; however, projects that are funded at 100% from the federal environmental cooperative agreement were being omitted. DMA agrees that all environmental projects should be entered into the FMS work order system and will begin entering and tracking all environmental projects in FMS immediately.*

##### **Auditor Reply**

We agree that DMA should continue to pursue, if practical, the creation of one work order system. Perhaps the PRIDE system will provide the avenue to meet this goal.

#### **FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures**

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State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 National Guard Program

Pass-Through Agency: U.S. Department of Defense

Compliance: Matching, Level of Effort, Earmarking

Amount of Questioned Costs: None

While testing the federal match rate for a random sample of 40 telecommunications expenditures recorded in object code E262, we noted five (5) expenditures (or 12.5% of the sample) where DMA did not apply the correct match rate.

The cause of the match rate errors is due to 1) changes in the federal match rates were likely not communicated to the appropriate MARS accounting personnel and 2) inadequate

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures (Continued)**

oversight of the E262 payment process. The effect is that the match rate for various activity codes in MARS was not updated timely and that the State paid for a larger share of expenditures than what was required for the items in our sample.

Section 201.b of Article II Obligations of the Parties of the Master Agreement states, “The state will obligate sufficient funds to pay its share of the costs of this MCA.” Section 202a also provides that the “NGB shall reimburse the State for the allowable costs incurred in performance of this MCA according to its terms and conditions for reimbursement.” Furthermore, to ensure compliance with the Master Agreement, good internal controls dictate accounts be set up correctly so that expenditures are funded from the appropriate sources. Should the funding for an activity code be changed, this change should be communicated to the appropriate personnel so that the activity code in MARS can be updated accordingly.

**Recommendation**

We recommend that Military Affairs 1) correct the funding structure for activity codes X623, X735, X845, X854, and X894, 2) periodically review all activity codes in MARS to ensure the funding is properly set up, 3) communicate match rate changes to the appropriate personnel and update the match rate in MARS timely for future changes in activity funding structures, and 4) maintain a log of the match rate changes (date of change, activity code, match rate, reason, approvals, etc.).

**Management Response and Corrective Action Plan**

*Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for allowable cost / cost principles is to provide reasonable assurance that Federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.*

*Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and has determined that DMA does not concur with the auditor's finding due to factual misstatements that occur in the auditor's finding.*

## FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures (Continued)**

##### **Management Response and Corrective Action Plan**

3. *FACT: In MARS, the cost split ratio is determined by the Project Billing setup table (PFST) not by the Activity Code. FACTUAL MISTATEMENT: The auditor states in the Cause and Effect paragraph, in the Criteria paragraph and in the Recommendation paragraph of the finding that the “match rate for various activity codes” and “activity funding structures” were not updated which caused an incorrect match rate to be applied resulting in a condition whereby “the State paid for a larger share of expenditures than what was required for the items in our sample”. Since the Activity Code has nothing to do with the split ratio of the cost in the MARS accounting system, this is categorically untrue.*

*EXPLANATION: In MARS Cost Accounting, a project is established with one or more sub-projects to track costs. But to obtain a fund split, each sub-project must have a split ratio established via PZ documents to effect the split. When an eligible cost is posted against the project / sub-project, the accounting system then splits that cost out into its state share and federal share based on the ratio data in the Project Billing (PFST) table. Activity Codes have no role in splitting out these costs into their constituent shares. DMA uses Activity Codes only for sorting financial or programmatic reports for federal reporting purposes and not for actuating cost splitting. DMA has historically used the text name field of the Activity Code to indicate to a person paying bills which sub-project the Activity Code should be used with and this percentile figure in the Activity Code name may have caused the auditor’s to assume that the Activity Code controlled the fund splitting.*

4. *FACT: All of the five invoices identified by the auditor as having incorrect match rates did execute the required match appropriately and in accordance with internal control federal billing rules within the MARS software system. FACTUAL MISTATEMENT: The auditor states in the Condition paragraph that “five expenditures” were found “where DMA did not apply the correct match rate”. In a subsequent email, these were identified by the auditor as:*

*I-04524636 dated 8/18/2004 against the AYCM4 federal agreement (Total AYCM497Z posted = \$142.22 which should split to \$137.95 federal share and \$4.27 state share)*

*I-04539225 dated 8/31/2004 against the AYCM4 federal agreement (Total AYCM497Z posted = \$39,256.76 which should split to \$38,079.06 federal share and \$1,177.70 state share; and Total AYCM450Z posted = \$1,300.89 which should split to \$650.45 federal share and \$650.44 state share)*

## FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

### *Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

#### **FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures (Continued)**

##### **Management Response and Corrective Action Plan**

*I-04581425 dated 9/29/2004 against the AYCM4 federal agreement (Total AYCM497Z posted = \$39,256.76 which should split to \$38,079.06 federal share and \$1,177.70 state share; and Total AYCM450Z posted = \$1,300.89 which should split to \$650.45 federal share and \$650.44 state share)*

*I-4675606 dated 12/7/2004 against the AYCM5 federal agreement (Total AYCM597Z posted = \$39,811.76 which should split to \$38,617.41 federal share and \$1,194.35 state share)*

*I-0496976 dated 12/22/2004 against the AYCM5 federal agreement (Total AYCM597Z posted = \$14,173.81 which should split to \$4,484.19 federal share and \$138.69 state share)*

*EXPLANATION: The federal grantor's representative and the state coordinator reviewed all the above invoices and found all were coded to the proper sub-project for cost splitting purposes. Data obtained from the MARS MRDB also found that three of the five invoices cited as incorrect did have the correct state match amount entered and transferred on the corresponding JV BX document which moves the state share from the original payment accounting string (1200 AYCM) to the accounting string for the state matching funds (0100 AYCM). The three correct original payment invoices and their corresponding JV BX documents are:*

*JV 095 BX082005080 dated 8/20/2004 reference I-04524636 moved \$4.26 from 1200 AYCM AYCM497Z to 0100 AYCM AYCM497Z.*

*JV 095 BX121018231 dated 12/10/2004 reference I-04675606 moved \$1,194.30 from 1200 AYCM AYCM497Z to 0100 AYCM AYCM497Z.*

*JV 095 BX122319561 dated 12/23/2004 reference I-04696976 moved \$138.69 from 1200 AYCM AYCM597Z to 0100 AYCM AYCM597Z.*

*The two remaining invoice payments (I-04539225 and I-04581425) did not split at an exact 97% ratio due to corrective entries made to the project billing setup.*

*JV 095 BX090306296 dated 9/3/2004 reference I-04539225 moved \$650.44 from 1200 AYCM AYCM50Z to 0100 AYCM AYCM50Z and \$958.99 from 1200 AYCM AYCM597Z to 0100 AYCM AYCM597Z.*

*JV 095 BX100109785 dated 10/1/2004 reference I-04581425 moved \$650.44 from 1200 AYCM AYCM50Z to 0100 AYCM AYCM50Z and \$958.99 from 1200 AYCM AYCM597Z to 0100 AYCM AYCM597Z.*

*The normal corrective action for an incorrect fund split error in MARS is to correct the amounts specified in the project billing setup and then let the accounting system 'catch-up' to the proper ratio. The proper ratio was, in*



**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS*****Other Matters Relating to Internal Controls and/or Instances of Noncompliance*****FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures (Continued)****Management Response and Corrective Action Plan**

*fact, achieved at the conclusion of the AYCM497Z (97%) grant award as evidenced by a federal share disbursed of \$580,000 and a state share disbursed of \$17,397.84 which achieved a final ratio of 97.0877296%.*

*CONCLUSION: In conclusion, DMA can find no evidence of an internal control problem in this finding and does not concur with the auditor's findings, conclusion or recommendation. The fundamental auditor's issue that, for two disbursements, the billing system was not matching at exactly a 97% ratio per disbursement is actually proof that corrective action was being implemented by the accounting system and that the end product, at the conclusion of the grant, was a 97% matching ratio. OMB Circular A-87, paragraph 24, Matching or cost sharing, does not require exact ratio matching per disbursement but only requires that the cost sharing ratio be achieved. Since the auditor did not check to see whether the required ratio had been achieved over the complete duration of the grant, the finding that DMA did not meet the matching ratio is not correct*

**Auditor Reply**

1. As discussed with DMA management, we are aware that the match is not driven by the activity code but is instead driven by the funding structure found in the sub-project field. The finding above discusses the activity coding in MARS because all of the DMA supporting worksheets were driven and classified by activity codes and that was the easiest way to communicate which sub-project funding codes were set up improperly in MARS. We also explained to DMA management that the percentage of funding displayed in the "Line Description" field for activity codes was not relied upon for testing. Instead, we examined the subproject field and verified the accuracy of the split by netting the original fund 1200 expenditure with the subsequent system generated BX document. This will be further explained in item two (2) below.
2. The specific exceptions were communicated via email to the audit liaison and the federal grantor representative on 2/15/06 and DMA had multiple opportunities to attempt to clear these exceptions prior to issuing this comment. Each exception was also discussed over the phone with the federal grantor representative who agreed that the funding was not set up properly in MARS. Only after the issuance of this finding

**FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

*Other Matters Relating to Internal Controls and/or Instances of Noncompliance*

**FINDING 05-DMA-14: The Department Of Military Affairs Should Ensure The State Match Rate Is Applied Correctly For All Program Expenditures (Continued)**

**Auditor Reply**

3. did DMA provide responses that cleared three of the five exceptions. The remaining two exceptions appear below:

ORIGINAL TRANSACTION	I-04675606	I-04696976
BX DOCUMENT	BX121018231	BX122319561
ORIGINAL EXPENDITURE	585.04	50.00
SUBSEQUENT BX DOCUMENT	(17.55)	(1.50)
NET CHARGE TO FUND 1200	567.49	48.50
% FEDERALLY FUNDED	97.0%	97.0%
% SHOULD BE FEDERALLY FUNDED PER FEDERAL GRANTOR'S REPRESENTATIVE	100.0%	100.0%
 SUB-PROJECT FIELD IN MARS FOR ACTIVITY CODE	 97	 97

With these two (2) items, we agree with DMA that MARS executed the split precisely the way the subproject field indicates. The true problem with these is a breakdown of communication between DMA and the federal grantor's representative. Specifically, the federal grantor's supporting documentation (that was obtained from DMA accounting personnel) indicated that the funding should be paid from 100% federal funds. Since the DMA accounting personnel had access to this worksheet, the funding structure for this (and possibly other activity codes) should have updated and corrected timely. Therefore, we again recommend that DMA management implement the items noted in the recommendation section above.

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Reportable Conditions</u></b>					
<b><i>(1) Audit findings that have been fully corrected</i></b>					
FY 04	04-DMA-01	The Department Of Military Affairs Should Develop Internal Control Procedures To Retain The Documentation Used To Compute The Payroll Cost Allocation Plan	12.401	0	Resolved in FY 05
FY 04	04-DMA-03	The Department Of Military Affairs Should Implement Internal Control To Retain Supporting Documentation For PX Documents	97.036	\$98,679	Resolved in FY 05
<b><i>(2) Audit findings not corrected or partially corrected:</i></b>					
FY 04	04-DMA-02	The Department Of Military Affairs Should Implement Internal Control Procedures To Comply With NGR 5-1/ANGI 63/101 Relating To Program Income For The National Guard Program	12.401	0	See 05-DMA-04
FY 03	02-MIL-2	The Department Of Military Affairs Should Ensure Subrecipient Monitoring Is Properly Performed	97.036	0	See 05-DMA-03
FY 02	02-MIL-1	The Department Of Military Affairs Should Ensure Subrecipient Monitoring Is Properly Performed	97.036	0	See 05-DMA-03
FY 01	01-MIL-1	The Department Of Military Affairs Should Ensure Subrecipients Meet OMB Circular A-133 Audit Requirements	97.036	0	See 05-DMA-03
FY 97	97-Military Affairs-50	The Department Of Military Affairs Should Strengthen Procedures For Monitoring Subrecipients	97.036	\$62,500	See 05-DMA-03
FY 00				-34,747	
FY 02				<u>-27,743</u>	
		Total Questioned Costs		0	

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**

**FOR THE YEAR ENDED JUNE 30, 2005**

**Reportable Conditions (Continued):**

*(3) Corrective action taken is significantly different from corrective action previously reported:*

No findings for this section

*(4) Audit Finding is no longer valid or does not warrant further action:*

No findings for this section

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
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**Material Reportable Conditions**

*(1) Audit findings that have been fully corrected*

No Finding for this section

*(2) Audit findings not corrected or partially corrected:*

FY 04	04-DMA-04	The Department Of Military Affairs Should Develop An Internal Control System For The State Domestic Preparedness Equipment Support Program To Comply With OMB Circular A-133 Compliance Requirements	97.004	0	Partially Resolved, Changed to Reportable Condition for FY 05 See 05-DMA-02
FY 04	04-DMA-05	The Department Of Military Affairs Should Follow Established Internal Control Used To Ensure Compliance With OMB Circular A-133 Compliance Requirements For The Public Assistance Program	97.036	0	Partially Resolved, Changed to Reportable Condition for FY 05 See 05-DMA-03

*(3) Corrective action taken is significantly different from corrective action previously reported:*

No findings for this section

*(4) Audit Finding is no longer valid or does not warrant further action:*

No findings for this section

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS**  
**FOR THE YEAR ENDED JUNE 30, 2005**

<b>Fiscal Year</b>	<b>Finding Number</b>	<b>Finding</b>	<b>CFDA Number</b>	<b>Questioned Costs</b>	<b>Comments</b>
<b><u>Other Matters</u></b>					
<b><i>(1) Audit findings that have been fully corrected</i></b>					
FY 04	04-DMA-08	The Department Of Military Affairs Should Improve Internal Controls To Ensure Local Governments Are Not Supplanting Federal Funds With Local Funds	97.004	0	Resolved for FY 05
FY 04	04-DMA-09	The Department Of Military Affairs Should Develop Written Procedures For The Work Order Process	12.401	0	Resolved for FY 05
<b><i>(2) Audit findings not corrected or partially corrected:</i></b>					
FY 04	04-DMA-06	The Department Of Military Affairs Should Establish Written Procedures For The Preparation Of The Quarterly SF-269 Report	97.004 & 97.036	0	97.004 Resolved, 97.036 Not Resolved - Changed to a Reportable Condition for FY 05 See 05-DMA-06
FY 04	04-DMA-07	The Department Of Military Affairs Should Improve Internal Controls Relating To Equipment Management	97.004	0	See 05-DMA-11
FY 04	04-DMA-10	The Department Of Military Affairs Should Improve Internal Controls Relating To The Review Process For The OJP 4578/1 Form Semi-Annual Report	97.004	0	See 05-DMA-12
<b><i>(3) Corrective action taken is significantly different from corrective action previously reported:</i></b>					
No findings for this section					
<b><i>(4) Audit Finding is no longer valid or does not warrant further action:</i></b>					
No findings for this section					

